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UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

Before The Honorable Yvonne Gonzalez Rogers, Judge

JAMES FABIAN,	)	
	)	
Plaintiff,	)	
	)	
VS.	)	<b>NO. CV 19-00054-YGR</b>
	)	
NANO F/K/A RAIBLOCKS F/K/A	)	
HIEUSYS LLC, ET AL.,	)	
	)	
Defendants.	)	
_____	)	

Oakland, California  
Tuesday, September 24, 2019

**TRANSCRIPT OF PROCEEDINGS**

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**BY: PAUL J. BYRNE, ESQUIRE**

Tuesday - September 24, 2019

2:00 p.m.

P R O C E E D I N G S

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**THE CLERK:** Calling CV 19-0054, Fabian vs. Nano f/k/a Raiblocks f/d/a Hieusys LLC, et al.

Counsel, please come forward and state your appearances.

**MR. CARRIEL:** John Carriel on behalf of Plaintiff Fabian.

**MR. FRIEDMAN:** Good afternoon, Your Honor. Todd Friedman also on behalf of the plaintiff.

**THE COURT:** Okay, Gentlemen. Good afternoon. Welcome to California.

**MR. FRIEDMAN:** Thank you.

**MR. CARRIEL:** Thank you.

**MR. SCHOOLIDGE:** Good afternoon, Your Honor. Peter Schoolidge for the defendants Heiusys LLC, Colin Lemahieu, Troy Retzer, and Mica Busch.

**MR. FOX:** Peter Fox for the same defendants.

**MR. BYRNE:** Good afternoon. Paul Byrne for the same defendants, Your Honor.

**THE COURT:** Okay. Good afternoon to you all as well.

All right. A written order will issue with respect to this matter, but let's go through it. We'll see where we end up.

You've already had one comprehensive hearing on the

1 matter, but given the significant changes in the Complaint, I  
2 thought it was worthwhile to have another hearing. You will  
3 not be allowed to so amend your Complaint again in this manner.  
4 You will only be allowed to amend it to the extent you're  
5 provided leave. Do you understand?

6 **MR. CARRIEL:** Yes, Your Honor.

7 **THE COURT:** All right. Before we get started, a  
8 procedural issue. What is the status of the other parties?  
9 Have they been served? That is Francesco Firano and BG  
10 Services.

11 **MR. CARRIEL:** Yes, Your Honor.

12 They have not been served yet. Our thinking was to see  
13 how the bankruptcy proceeding played out in Italy, and it has  
14 concluded, and at this point, since he has been declared  
15 bankrupt, we're not sure that it would be in the best interests  
16 to serve him as it would only further deplete any of the  
17 potential funds recovered for the class because he would likely  
18 use BitGrail funds to defend that action.

19 **THE COURT:** So what are you going to do with him?

20 **MR. CARRIEL:** It depends on the outcome of this  
21 proceeding, Your Honor.

22 **THE COURT:** All right.

23 So let's start with the federal securities claims. Again,  
24 I think everyone understands that Section 15(a), that claim  
25 rises and falls with Section 12; correct?

1           **MR. CARRIEL:** Yes, Your Honor.

2           **MR. SCHOOLIDGE:** Yes, Your Honor.

3           **THE COURT:** And it doesn't look to me as if you  
4 provided me, frankly, with any more authority on this notion of  
5 whether claims under the statute can be tolled, that is, the  
6 statute of limitations, so I think my earlier analysis would  
7 be, as I mentioned the first time -- which is to follow the  
8 First, Second, Third, Fifth, Sixth, and Eighth Circuits and  
9 find that the equitable tolling does not apply. And if that's  
10 the case, then with respect to those claims, it appears to me  
11 that they are barred by the statute of limitations.

12           **MR. CARRIEL:** Your Honor, we would argue that if that  
13 is the case, that Plaintiff Fabian's claims should continue  
14 under *American Pipe*. They should still be tolled.

15           **THE COURT:** You mean individually?

16           **MR. CARRIEL:** Yes, Your Honor.

17           **THE COURT:** Well, how, again, would -- well, a  
18 response.

19           **MR. FOX:** Your Honor, we argued in our motion papers  
20 that --

21           **THE COURT:** Let me ask -- usually, Mr. Fox, I don't  
22 have defense counsel gang up on plaintiff's counsel, so are you  
23 going to tell me in advance who is taking which issues?

24           **MR. FOX:** Certainly, Your Honor. I'm going to handle  
25 timeliness; and to the extent that it becomes relevant for the

1 purposes of this argument, *Howey*; and I will also handle the  
2 implied contract claim; the fraud claim; the negligent  
3 misrepresentation claim; and the unjust enrichment claim.

4 My partner, Mr. Schoolidge, will handle statutory standing  
5 under 12(a)(1); *Morrison*, again to the extent that those even  
6 become relevant for the purposes of the argument; negligence;  
7 breach of fiduciary duty; constructive fraud; and aiding and  
8 abetting breach of fiduciary duty.

9 **THE COURT:** Okay. Thank you. Go ahead.

10 **MR. FOX:** So the *American Pipe* tolling doctrine is an  
11 equitable doctrine. It doesn't apply as a matter of right, and  
12 there is authority for that in our opening brief in support of  
13 the motion.

14 In cases where the plaintiff is responsible for his own  
15 prejudice, such as the *Weitzner* case which we cited from the  
16 Third Circuit in our opening brief, tolling for individual  
17 claims has been denied under *American Pipe*.

18 Those arguments were set forth in the opening brief, and  
19 the Plaintiffs did not respond to those arguments in their  
20 opposition.

21 It's our view that under applicable case law in this  
22 circuit and in this district, they've waived any argument to  
23 the contrary.

24 **THE COURT:** Response on the legal issues, not the  
25 waiver.

1           **MR. CARRIEL:** There are not any facts in this case  
2 to -- that indicate that plaintiffs -- that plaintiff is  
3 responsible for any untimeliness here. There is none set forth  
4 in the Complaint, there is none in the opposition --

5           **THE COURT:** Well, it's your obligation affirmatively  
6 to make sure that your claim falls within the applicable  
7 statute of limitations. This issue was raised on the first  
8 round. You had notice of it at the first round, and you need  
9 to plead facts to show that the claim should proceed.

10           **MR. CARRIEL:** The facts that we plead in the Complaint  
11 and in our opposition to the renewed motion to dismiss are  
12 that, first, the claims were filed only 22 days after the  
13 statute of limitations would have been -- would have expired.

14           Second, the Nano defendants took concerted efforts to  
15 delay the filing of timely claims in this case in that they  
16 settled with the first putative class action representative  
17 that filed the *Brola* case in the Southern District of New York  
18 and they funded \$1 million towards a legal fund in Italy to  
19 pursue the Italian bankruptcy proceedings.

20           These facts lend toward the idea that the Nano  
21 development -- developers took efforts to delay the filing of a  
22 more timely claim.

23           **THE COURT:** Well, okay.

24           A response.

25           **MR. FOX:** Your Honor, we're not aware of any case law

1 and the plaintiff hasn't cited to any indicating that any of  
2 those facts are relevant for the purposes of *American Pipe*  
3 tolling.

4 For the purposes of *American Pipe* tolling, what's relevant  
5 is whether the plaintiff was a member of the putative class in  
6 the predecessor class action, and as in the case of *Weitzner*,  
7 whether either on his own or through -- we would argue through  
8 his agent he was able to participate in that class action.

9 **THE COURT:** Okay. Well, let's move on.

10 With respect to the state law claims -- we'll go through  
11 this. Defendants have asked that I exercise supplemental  
12 jurisdiction. Would there be a basis for jurisdiction under  
13 CAFA? I thought it was pled.

14 **MR. FOX:** I believe you're correct, Your Honor.  
15 Because of the size of the class action, there may be a basis  
16 for jurisdiction -- for original jurisdiction over these state  
17 law claims.

18 **THE COURT:** Okay.

19 The breach of the implied contract claim. Again,  
20 Mr. Carriel, it seems to me at most what you have here is a  
21 relationship, but a relationship does not in and of itself give  
22 rise to mutual assent, to an implied contract.

23 There's a relationship with us here in the courtroom.  
24 We're all related to, you know -- we're all coming together  
25 with respect to this action. That doesn't mean there's



1 contracts. So just because parties are in the room, so to  
2 speak, doesn't mean that there is a contract or an implied  
3 contract. And that seems to be all you really have, which  
4 isn't sufficient.

5 Any comments?

6 **MR. CARRIEL:** Your Honor, we argue in our opposition  
7 to the motion to dismiss that the Nano developers' actions and  
8 conduct gave rise to implied contracts, and these actions  
9 specifically were they developed and marketed XRB, they created  
10 the BitGrail Exchange with Defendant Firano and maintained its  
11 operations alongside him, and that implied --

12 **THE COURT:** None of what you have just said  
13 articulates the terms of a contract.

14 **MR. CARRIEL:** Fair enough, Your Honor. And if that is  
15 the case, these facts certainly articulate the existence of a  
16 relationship that was breached, so it would roll into our  
17 fiduciary duty claims.

18 **THE COURT:** All right. Well, I don't think you have a  
19 breach of contract claim. Similarly, I don't think you have  
20 alleged the breach of fiduciary duty. You keep talking about  
21 custodianship.

22 There is law in California, specific law, about what the  
23 elements of a fiduciary duty are, and this reference to  
24 "custodianship" isn't -- it's just a word, actually, without  
25 any kind of legal meaning that doesn't satisfy the existence

1 of -- or that doesn't satisfy each of the elements.

2 So before you can have a breach, you have to have the  
3 existence of a duty. And, again, just because people have some  
4 relationship or connection or are in the room, as they say,  
5 that doesn't create a fiduciary duty.

6 People try to argue fiduciary duty in all sorts of  
7 contexts; for instance, banking context. It doesn't apply.  
8 It's just that's what the law is. You have to have a special  
9 kind of relationship that creates the duty based upon case law,  
10 and I'm not seeing that you've been able to do that.

11 Any comments?

12 **MR. CARRIEL:** We allege that the duty that was created  
13 here could be one of two things. It could be either the Nano  
14 developers' creation and control over the XRB protocol, which  
15 is the code that --

16 **THE COURT:** I don't want to talk about breach. I want  
17 to talk about --

18 **MR. CARRIEL:** The duty.

19 **THE COURT:** -- the duty and how the duty between  
20 particular players is created. So, for instance, a trustee has  
21 a special relationship with a beneficiary of the trust.  
22 There's a lot of case law on that. Those are the two different  
23 players.

24 Here you have a commercial context, a buyer and a seller.  
25 There's no fiduciary duty between a buyer and a seller. How is

1 this any different?

2 **MR. CARRIEL:** The seller here wasn't just a seller.  
3 It was also the creator of the Exchange and --

4 **THE COURT:** What kind of law do you have to support  
5 your notion that the maker of an exchange who is a seller of  
6 components for that exchange -- how that creates the existence  
7 of a fiduciary duty? I need law. If you don't have law and  
8 you don't have some way of extending existing law on the duty  
9 issue, then, again, I don't know how you can succeed.

10 **MR. CARRIEL:** Our opposition cites to *Los Angeles*  
11 *County Employees Retirement Association vs. Bank of New York*  
12 *Mellon Corporation*. And in that case, the court held that the  
13 key factor in the existence of a fiduciary relationship lies in  
14 the control by a person over the property of another.

15 And here that control was -- that is on page 18 and 19 of  
16 our opposition brief. And in this case, that control is the  
17 Nano developers' control over the XRB protocol or control over  
18 BitGrail such as when they exercise that control to prevent  
19 Defendant Firano from shutting down the Exchange.

20 **THE COURT:** Response.

21 **MR. SCHOOLIDGE:** Your Honor, I think what they're  
22 asking for here is a ruling that would expand the fiduciary  
23 duty to anyone who ever developed software that was later used  
24 by someone down the road in some attenuated way and a problem  
25 happened.

1           The defendants are not alleged to have had control over  
2           the specific deposit that Mr. Fabian made. They didn't have  
3           control over the software that BitGrail operated. They wrote  
4           some code a while back and then put it out there in the world,  
5           and it was used by third parties, and that's not, under  
6           California law, what gives rise to a fiduciary duty. There is  
7           no knowing undertaking by the defendants of a fiduciary  
8           relationship, and there is no relationship that, as a matter of  
9           law, imposes a fiduciary duty here. There is no relationship.

10           **THE COURT:** And your response to the case authority  
11           cited?

12           **MR. FOX:** If I may, Your Honor, I'm familiar with the  
13           case. That's the FX litigation.

14           **THE COURT:** Okay. Didn't I just say that I wasn't  
15           going to allow you to double team?

16           **MR. FOX:** You're right.

17           **MR. SCHOOLIDGE:** So, Your Honor, in that case, there  
18           was actually custodianship because the plaintiffs had deposited  
19           money with a third party.

20           Here the third party is not the defendants. The third  
21           party is another party that is named as a defendant in this  
22           case but hasn't been served and is just really a phantom party.

23           **THE COURT:** Okay.

24           Any response?

25           **MR. CARRIEL:** Defense counsel argues that there are no

1 facts lending towards the idea that the Nano developers assumed  
2 any of -- any responsibilities or any special relationship or  
3 duties to plaintiff investors, but that's just not the case.

4 The Amended Complaint alleges that --

5 **THE COURT:** What paragraph?

6 **MR. CARRIEL:** Paragraph 88.

7 **THE COURT:** I don't see where it does that in  
8 paragraph 88.

9 **MR. CARRIEL:** It's on page 20 inside the image. The  
10 last -- second to the last line inside there is, "We're  
11 investigating creating an irrevocable trust to document our  
12 commitment to the distribution." So there's that.

13 And in addition to that, we also allege that the Nano  
14 developers acknowledge the need to conduct a security audit  
15 over the Nano protocol, which is the protocol that was lacking  
16 safeguards which caused the loss of the funds in this case.  
17 And that's --

18 **THE COURT:** What paragraph?

19 **MR. CARRIEL:** -- paragraph 140 to 141.

20 And on top of all of that, the Nano developers took it  
21 upon themselves to spend \$1 million to fund the bankruptcy  
22 proceeding --

23 **THE COURT:** Where is that?

24 **MR. CARRIEL:** That is paragraph 12.

25 **THE COURT:** I don't understand how that -- I don't

1 understand how what they did in paragraph 12 has anything to do  
2 with the creation of a fiduciary duty between the plaintiff and  
3 the defendant.

4 **MR. CARRIEL:** Those actions --

5 **THE COURT:** The existence of a fiduciary duty exists  
6 because of the parties' relationship to each other, not because  
7 of some action with respect to a non-party.

8 **MR. CARRIEL:** Well, the non-party isn't an  
9 unaffiliated entity. The non-party in this case is BitGrail  
10 and Firano, and as --

11 **THE COURT:** I need you to look objectively -- to  
12 answer my question objectively. I understand, again, that  
13 people are related. They're in the room. That's not the  
14 question.

15 The question is from an objective point of view, what is  
16 it about the relationship between the plaintiff and these  
17 defendants, and you give me paragraphs 80, 140, and 141. I'll  
18 go back and look at those. But how they're dealing with some  
19 other party, whether or not they had any involvement, I don't  
20 understand how that objectively helps your -- articulate what  
21 the relationship is.

22 **MR. CARRIEL:** The relationship here is their creation  
23 of XRB and the XRB protocol or --

24 **THE COURT:** So are you saying that any software  
25 developer has a fiduciary duty?

1           What would the law exam look like based upon your -- I'm  
2           trying to get you to articulate something objectively. What  
3           does it look like? Software developer and a purchaser? What  
4           is it?

5           **MR. CARRIEL:** I would argue that in certain cases,  
6           such as this one, a software developer can have duties to their  
7           purchasers which would arise from the software developer  
8           describing their software and saying that it works a certain  
9           way and that it has certain safeguards and security  
10          implementations when, in fact, it does not.

11          **THE COURT:** So if you buy an app and because you  
12          bought the app on your phone and somehow a bug goes through and  
13          messes up your calendaring system through the app, all of a  
14          sudden, a software developer is going to have a fiduciary duty  
15          to the purchaser because that software developer said it was  
16          secure and it wasn't?

17          **MR. CARRIEL:** Not necessarily --

18          **THE COURT:** Okay. Well, then what is it about the  
19          relationship between a software developer and a purchaser that  
20          creates a fiduciary duty, objectively speaking?

21          **MR. CARRIEL:** What makes this case different is  
22          that --

23          **THE COURT:** What makes it different objectively,  
24          period, in all cases such as these?

25          **MR. CARRIEL:** These were investments, not the use of

1 an app.

2 **THE COURT:** So a purchaser -- an investor. So you're  
3 saying a software developer and an investor, through the  
4 developer's product, is what creates a fiduciary duty?

5 **MR. CARRIEL:** Investment in the developer's product  
6 rather than through it.

7 **THE COURT:** Any response?

8 **MR. SCHOOLIDGE:** Your Honor, there was no allegation  
9 of an investment in the developer's product.

10 Mr. Fabian bought the coins from third parties that are  
11 not even alleged in the Complaint -- we don't know who they  
12 were -- on an exchange in Italy from someone who's not even in  
13 the case, and there were no sales from the Nano defendants to  
14 anyone. They didn't sell software.

15 **THE COURT:** The reference to paragraphs 88, 140, and  
16 141, any comments?

17 **MR. SCHOOLIDGE:** Your Honor, with regard to 88 -- I'm  
18 just looking at it -- I think that in fact it proves the  
19 opposite of what they are saying. It says, "We are  
20 investigating creating an irrevocable legal trust," not that  
21 they have created one, in which case that would perhaps give  
22 rise to a fiduciary duty.

23 The others I think we pretty much covered in our papers,  
24 Your Honor.

25 **THE COURT:** Okay. Any final comments?



1           **MR. CARRIEL:** Your Honor, I would also like to point  
2 to paragraphs 116, 168, and 142.

3           116 deals with the Nano developers giving investment  
4 advice. 168 deals with the Nano developers claiming that  
5 BitGrail was safe. We argue that this gives rise to a breach  
6 of fiduciary duty because the Nano developers had inside  
7 confidential information through their control over BitGrail,  
8 information that revealed that BitGrail was, in fact, not safe,  
9 yet they were publicly telling investors that it was safe.

10          **THE COURT:** Any response?

11          **MR. SCHOOLIDGE:** At bottom, the fiduciary duty is  
12 about relationships of trust and confidence between parties.  
13 There was no relationship whatsoever between Mr. Fabian and  
14 these defendants.

15          **THE COURT:** Okay. Everybody agrees the aiding and  
16 abetting a fiduciary duty rises and falls with the breach of  
17 fiduciary duty?

18          **MR. SCHOOLIDGE:** Agreed, Your Honor.

19          **MR. CARRIEL:** Yes, except that the breach of fiduciary  
20 duty would be BitGrail's breach rather than the Nano  
21 defendants' breach.

22          **THE COURT:** Well, the fiduciary duty claim is brought  
23 against all defendants, not just the BitGrail defendants.

24          **MR. CARRIEL:** Yes, Your Honor.

25          **THE COURT:** Why --

1           **MR. CARRIEL:** Except the aiding and abetting breach of  
2 fiduciary duty is brought against the Nano defendants for  
3 aiding and abetting the BitGrail defendants' breach of  
4 fiduciary duty, which is --

5           **THE COURT:** Oh, I see what you're saying. Okay.

6           Now, with respect to negligence, negligence, unlike  
7 fiduciary duty, is a much more generic tort, and it's very  
8 broad.

9           As I look at the five different factors or six different  
10 factors that exist under *Rowland vs. Christian*, California  
11 Supreme Court case from 1968, which is the seminal case on this  
12 topic, five of the six factors seem to suggest that there is a  
13 duty.

14           The only thing, frankly, that is potentially missing here  
15 is causation; that is, that the Complaint doesn't really  
16 provide any facts to suggest causation, and a legal conclusion  
17 in paragraph 230 is not enough.

18           So first on the overview, we'll start with the defendants.  
19 Who is doing this one? Mr. Fox?

20           **MR. FOX:** Mr. Schoolidge will be handling negligence.

21           **THE COURT:** Okay.

22           **MR. SCHOOLIDGE:** We kind of had to pick what to focus  
23 on for this one because there are so many claims in the  
24 Complaint and so many arguments being made, page limit being  
25 what it is, so we focused on proximate cause, but we don't

1 think there is a duty alleged either. A lot of the stuff that  
2 they allege as a duty are just pretty much anything that had to  
3 do with the coin or anything that the defendants were doing.  
4 For example, you know, developing the XRB protocol is alleged  
5 to be a duty or maintaining it is alleged to be a duty. Why,  
6 I'm not sure. It's not pled in the Complaint. They don't  
7 explain it in the opposition brief.

8 But turning to proximate cause, I think it's pretty clear  
9 that there were a lot of things that happened between my  
10 clients developing this Nano protocol and Mr. Fabian losing his  
11 coins.

12 Francesco Firano came along --

13 **THE COURT:** Once you start arguing the facts, you  
14 lose. This is a motion to dismiss. It's not summary judgment.  
15 In a motion to dismiss, I accept the facts in the Complaint as  
16 true and any plausible inferences which inure to the benefit of  
17 the plaintiff, not the defense. You are arguing facts.

18 **MR. SCHOOLIDGE:** Well, I'm not arguing facts. These  
19 facts are in the Complaint. They allege that Francesco  
20 developed BitGrail. They allege that --

21 **THE COURT:** You started your sentence by saying, "It's  
22 pretty clear that there were a lot things happening between my  
23 clients developing the Nano protocol and Mr. Fabian losing his  
24 coins."

25 **MR. SCHOOLIDGE:** In the Complaint. There is

1 allegations of things --

2 **THE COURT:** Right. That's my point, is you're arguing  
3 the facts in the Complaint and what is it that ultimately  
4 results in causation as opposed to a lack thereof, any  
5 allegation, which is where I was going.

6 **MR. SCHOOLIDGE:** Well, there is no connection -- there  
7 is no allegation that my clients caused the loss. There is  
8 allegations of what happened between my clients developing the  
9 protocol and the loss happening, but I think that those  
10 allegations show pretty clearly that my clients were not close  
11 in proximity either in terms of events or time to Mr. Fabian's  
12 loss.

13 **THE COURT:** All right.

14 A response.

15 **MR. CARRIEL:** The causation here is the double  
16 withdrawals that occurred which is what permitted certain  
17 anonymous users to steal 170-million worth of XRB from  
18 BitGrail. They exploited a fault in the XRB code which was  
19 developed by the Nano developers and maintained by the Nano  
20 developers, so the causation here is they failed to enact  
21 adequate security measures in the Nano protocol which caused  
22 the theft of 170 million XRB.

23 **THE COURT:** What paragraph?

24 **MR. CARRIEL:** 160 and 171 as well.

25 **THE COURT:** And what?

1           **MR. CARRIEL:** 171.

2           **THE COURT:** Okay.

3           Any response on those two paragraphs?

4           **MR. SCHOOLIDGE:** So paragraph 160 contains many  
5 paragraphs quoting from the Italian bankruptcy court opinions,  
6 which in turn found that Mr. Firano was faulty in his  
7 development of the platform such that it would send individual  
8 requests that appeared to the Nano Node to be separate requests  
9 for identical amounts, thus causing the Nano Node to provide  
10 withdrawals to users that were not entitled to them. That's a  
11 lot of intervening cause that they don't explain.

12           **THE COURT:** Well, they don't have to. The question is  
13 is there a plausible connection.

14           Any comment on 171?

15           **MR. SCHOOLIDGE:** I would say that, Your Honor, 171 is  
16 just completely 180 degrees contradicted by the other material  
17 that they incorporate by reference in their Complaint and rely  
18 on heavily.

19           The Italian bankruptcy court found in fact that Mr. Firano  
20 was responsible. He made these same arguments to the court,  
21 and the court rejected them based on expert witness findings  
22 that were extensive.

23           **THE COURT:** Well, I don't know anything about Italian  
24 courts, so just because some court makes some finding, even a  
25 United States court -- just because they make a finding doesn't

1 mean any court is bound by that unless it's the Supreme Court  
2 or the circuit court in the same case.

3 **MR. SCHOOLIDGE:** Your Honor, I'm not saying that the  
4 Court is bound by it, but what we're saying is that they  
5 incorporated by reference into their Complaint as true facts,  
6 and they can't just selectively pick some little pieces that  
7 sound like they help them and then ignore the rest of it when  
8 they've incorporated it by reference. I mean, it's just before  
9 the Court as they're pleading. We're not asking for any kind  
10 of a ruling on whether the Court should accept those opinions  
11 as binding or anything like that. This is just stuff they put  
12 in their Complaint that contradicts the attorney argument they  
13 put in their Complaint.

14 **THE COURT:** Any response?

15 **MR. CARRIEL:** Your Honor, just because the Complaint  
16 contains several paragraphs from the Italian bankruptcy  
17 proceedings does not mean that we incorporate by reference the  
18 entirety of the Italian bankruptcy proceedings. The arguments  
19 that Defense counsel is putting forth are all factual arguments  
20 and --

21 **THE COURT:** Well, then articulate the causation. If  
22 you have contradictory paragraphs, I need an articulation of  
23 causation; otherwise, the claim fails.

24 **MR. CARRIEL:** Your Honor, in the Complaint, we do not  
25 have contradictory paragraphs. Defense counsel is reading

1 paragraphs that were not cited in the Complaint. They're  
2 reading them from the Italian bankruptcy proceeding as a whole.  
3 Those are not in the Complaint. There's nothing contradictory  
4 about our discussion of causation.

5 **THE COURT:** Okay. Well, then, make clear what your  
6 argument is so he can respond.

7 **MR. SCHOOLIDGE:** My argument? Well, Your Honor, my  
8 argument is that the entirety of the Italian bankruptcy  
9 opinions made quite clear, based on expert findings, that what  
10 happened was --

11 **THE COURT:** Are those opinions in this Complaint  
12 and -- or have you asked for judicial notice or something? If  
13 not, I can't refer to them.

14 **MR. SCHOOLIDGE:** Your Honor, we do in our opening and  
15 *Davis vs.* --

16 **THE COURT:** Not a brief. I need it in the Complaint  
17 or I need to have taken judicial notice for me to -- you  
18 can't -- you can't just refer to things outside the context of  
19 the pleadings in a Rule 12 motion.

20 **MR. SCHOOLIDGE:** Understood, Your Honor. We did note  
21 that there was extensive quoting of the opinions in our opening  
22 brief, and we asked the Court to take judicial notice of the  
23 entire opinions, and we attached them as exhibits.

24 *Davis vs. HSBC* is the precedent we cite for the  
25 proposition that the Court can consider them.

1           **THE COURT:** Well, let's talk about judicial notice.  
2 Is it proper or not? Did you oppose?

3           **MR. CARRIEL:** We did, Your Honor. Well, so defense  
4 attached the Italian bankruptcy -- well, translated versions of  
5 the Italian bankruptcy decisions to its motion to dismiss. We  
6 opposed that on the basis that --

7           **THE COURT:** What law?

8           **MR. CARRIEL:** -- they were not authenticated.  
9 I'm sorry?

10          **THE COURT:** First of all, is it improper as a matter  
11 of law to take judicial notice, or are you solely resting on  
12 authentication?

13          **MR. CARRIEL:** Our opposition solely rested on  
14 authentication. However --

15          **THE COURT:** Okay. So are you concerned that it is not  
16 authentic? Do you have a different version of that decision?

17          **MR. CARRIEL:** We do not, Your Honor. Now, we've  
18 become aware of the fact that the Italian -- the attorney in  
19 the Italian bankruptcy proceeding attached an affidavit to the  
20 reply in further support of the motion to dismiss  
21 authenticating the translations which we believe only further  
22 lends to the notion that the Nano developers are -- have been  
23 behind the Italian bankruptcy proceedings this entire time,  
24 when coupled with the \$1 million that they put toward funding  
25 it.



1           **THE COURT:** Back to the contradiction argument. So do  
2 I have -- I don't know that I have clarity on the issue.

3           **MR. FOX:** Your Honor, if I may be heard on the  
4 question of incorporation by reference?

5           **THE COURT:** Well, I know how to incorporate by  
6 reference.

7           **MR. FOX:** On the question as to whether it's proper  
8 on -- in this case.

9           **THE COURT:** It doesn't sound like he's got a real  
10 argument with respect to that topic. At first he said  
11 authentication. Then you provided the authentication. So now  
12 I'm looking for clarity on the contradiction that is alleged by  
13 the defense.

14           **MR. SCHOOLIDGE:** The contradiction is that they're  
15 claiming that the breaches of some duties that are not totally  
16 clear by the defendants were the cause of Mr. Fabian's loss,  
17 but the Italian bankruptcy opinion goes through in great detail  
18 and addresses how in fact this came about, and it's that  
19 Francesco Firano, when he set up the BitGrail --

20           **THE COURT:** Hold on a minute because I'm told that you  
21 did not submit a request for judicial notice. What document  
22 number is your request for judicial notice?

23           **MR. FOX:** Your Honor, I believe that was a  
24 misstatement. There was no formal motion requesting judicial  
25 notice. The argument for -- that the Court should review the

1 Italian bankruptcy opinions under the doctrine of incorporation  
2 by reference appears in footnote 3 of our reply which cites the  
3 *Davis vs. HSBC* and to *Doe 1 vs CVS Pharmacy*.

4 It's not our understanding that where a document has been  
5 heavily relied upon and, in this case, excerpted multiple times  
6 in the pleading that a separate request for judicial notice is  
7 required. Our understanding based on *Davis vs. HSBC* is that  
8 the Court may -- may; it's discretionary -- treat those  
9 materials that are incorporated by reference as part of the  
10 Complaint and assume that all the facts that appear in those  
11 materials are true. And I'm looking at page 1160 in the *Davis*  
12 *vs. HSBC* case.

13 **THE COURT:** I'll take a look at that. I was with you  
14 up until the end. I don't think anyone at a pleading stage has  
15 to accept things necessarily as true, especially when we have  
16 securities cases where people want to attach all sorts of  
17 things like articles and everything else. We don't do that.  
18 But I'll take a look at *Davis*.

19 All right. Back to your articulation.

20 **MR. SCHOOLIDGE:** So the expert witness that the court  
21 retained in the Italian bankruptcy court opinion found that  
22 Mr. Firano set up the BitGrail Exchange such that all the coins  
23 in everyone's account would be pooled into one wallet, one  
24 cryptocurrency wallet, and that whenever there was a request to  
25 withdraw by a user, it would be drawn from that wallet.

1           And Mr. Firano, when he would make a request to the Nano  
2     Node to withdraw coins for a user, would send a unique  
3     transaction identifier each time to the Nano Node. So for all  
4     the Nano Node knew, these were uniques transactions that were  
5     being made for the first time and were not double withdrawals.

6           And the court actually found to the contrary, explicitly  
7     said that the Nano defendant -- the Nano parties were not at  
8     fault. It was Mr. Firano's mismanagement of the platform that  
9     he had set up and his failure to have a proper accounting  
10    system that was the cause of the losses and then also third  
11    parties finding that out and exploiting it.

12          So how -- I'm saying how can there be proximate cause  
13    between the Nano defendants developing a protocol, you know,  
14    years earlier, putting it out in the world, and then Mr. Fabian  
15    losing his coins when there were all these things that happened  
16    in between there that contradict any conclusion that there was  
17    proximate cause by these defendants.

18           **THE COURT:** All right.

19          Now respond, assuming for purposes of argument,  
20    Mr. Carriel, that I do review that opinion and incorporate it  
21    by reference given your reference to it in the Complaint.

22           **MR. CARRIEL:** First, Your Honor, the Italian  
23    bankruptcy court did not find that the Nano developers were not  
24    at fault. That was just not a finding in either of the  
25    opinions.

1           **THE COURT:** All right. So let's just resolve that  
2 issue.

3           So Docket 64-1, Mr. Schoolidge, what page?

4           **MR. SCHOOLIDGE:** So, Your Honor, this is not  
5 paginated, but if you can --

6           **THE COURT:** I have an ECF number. Oh, I see. So  
7 I'm -- well, no, I do have a document. This has an ECF number.  
8 I see all the Italian.

9           **MR. SCHOOLIDGE:** It's page 15 of the --

10          **MR. FOX:** Your Honor, if I may, the translated version  
11 was attached as an exhibit to the Memorandum of Law that was  
12 filed on August 16th, I believe, and the relevant passage is  
13 in --

14          **THE COURT:** Hold on. Which is the docket number?  
15 Docket 60?

16          **MR. FOX:** Yes. It would be --

17          **THE COURT:** So it's 60-1?

18          **MR. FOX:** 60-1.

19          **THE COURT:** All right. Twenty-two pages --

20          **MR. FOX:** Correct.

21          **THE COURT:** -- of the ECF. So what page number?

22          **MR. FOX:** Page number 15.

23          **THE COURT:** Of 22.

24          **MR. FOX:** Correct. This should be the page that  
25 begins at the top with italicized text in the middle of a

1 sentence that reads, "with the Nano development team within  
2 which Firano had entered into December 2016 and exited December  
3 2017."

4 **THE COURT:** My page 15 of 22, the very first line  
5 begins with the phrase, "During the assessment carried out."  
6 Is that the same page?

7 **MR. FOX:** Then we're on 16.

8 **THE COURT:** Page 16 of 22 starts that with, "The  
9 development team within which" -- that one?

10 **MR. FOX:** Correct.

11 **THE COURT:** That's page 16 of 22, Docket 60-1. So --

12 **MR. SCHOOLIDGE:** So then, Your Honor, about seven  
13 lines up from the bottom --

14 **THE COURT:** Okay.

15 **MR. SCHOOLIDGE:** -- reads, "Therefore, it was the  
16 BitGrail Exchange that actually requested to the node multiple  
17 times to allow the funds to leave the wallet (funds that, in  
18 fact, had already left the account after the first request and  
19 not the Nano network that allowed the multiple withdrawals),"   
20 period.

21 **MR. FOX:** That's also on page 1 of our opening brief.

22 **THE COURT:** All right.

23 Mr. Carriel?

24 **MR. CARRIEL:** Your Honor, the Italian bankruptcy  
25 decisions also have language that explicitly explain that the

1 issue here was the Nano Node lacking the idempotence safety  
2 feature.

3 **THE COURT:** All right. What page?

4 **MR. CARRIEL:** We quoted within the Complaint --

5 **THE COURT:** No. Just give -- I'm going to go -- one  
6 of the things that you learn as a judge is to always take what  
7 lawyers say with a grain of salt and go to source material. So  
8 I'll be going to the source material.

9 Where in the source material is that?

10 **MR. CARRIEL:** In addition to this quotation, which I  
11 am currently looking for, this entire argument is undercut by  
12 the fact that the Nano development team adopted idempotence on  
13 February 16, 2018, two days after the hack was announced.

14 **MR. SCHOOLIDGE:** Your Honor, evidence of subsequent  
15 remedial measures is not admissible to prove liability.

16 **THE COURT:** We're not at a proof stage. We're at a  
17 pleading stage.

18 **MR. FOX:** If I may, Your Honor, just on --

19 **THE COURT:** Hold on.

20 **MR. CARRIEL:** This is not the exact quote that I was  
21 referring to, but something similar. Page 4 of 60-1.

22 **THE COURT:** Okay. Go ahead.

23 **MR. CARRIEL:** The last bullet point before the last  
24 paragraph on that page.

25 **THE COURT:** That they acknowledged the software flaws

1 after initially denying them?

2 **MR. CARRIEL:** Yes, Your Honor. The software flaws  
3 that they're referring to is the lack of idempotence in the  
4 Nano protocol.

5 The point here, Your Honor, is that the bankruptcy  
6 proceedings have language that can be cited to to support the  
7 notion that the Nano developers were entirely at fault. It  
8 also has language that can be cited to to support the notion  
9 that Firano was at fault, but these should be taken with a  
10 grain of salt because the bankruptcy proceedings were about  
11 Firano and BitGrail, not about the culpability of the Nano  
12 defendants, which we argue in our opposition to the motion to  
13 dismiss.

14 Moreover, at the motion to dismiss stage, all facts should  
15 be drawn, as you mentioned earlier, in the light most favorable  
16 to plaintiffs, not defendants. What defendants are arguing  
17 here is essentially trying to draw the light -- draw these  
18 facts --

19 **THE COURT:** To the extent that I think you don't have  
20 sufficient facts on causation, what else can you allege in the  
21 Complaint?

22 **MR. CARRIEL:** In addition to the Nano protocol, there  
23 is the fact that we allege that the Nano developers created  
24 BitGrail alongside Firano and managed its operations with  
25 respect to XRB such as when they prevented Firano from shutting

1 down the BitGrail exchange when he warned them that there was  
2 an issue that these funds were going missing.

3 Their prevention of BitGrail from shutting down caused the  
4 loss of tens of millions of dollars worth of XRB because, as we  
5 allege, they were first informed of the issue with the double  
6 withdrawal transactions in July of 2017, and these transactions  
7 continued to occur for another seven, eight months.

8 **THE COURT:** Okay. We're going to keep moving here.

9 **MR. SCHOOLIDGE:** Your Honor, just before we move on,  
10 could I just draw the Court's attention to the fact that  
11 Mr. Carriel just stood here and read language from page 4 of  
12 that opinion that is a summary of the arguments that Mr. Firano  
13 made that were rejected by the court?

14 **THE COURT:** All right. Noted.

15 **MR. SCHOOLIDGE:** Thank you.

16 **THE COURT:** We now move to negligent  
17 misrepresentation.

18 So one of the questions I have with respect -- I'm sorry.  
19 I missed fraud. Let me go to fraud first.

20 I think the key amendment to the Complaint with respect to  
21 fraud is plaintiff's allegations that he relied on the false  
22 representations and statements in holding on to his XRB on the  
23 Exchange. That's different than before.

24 It looks to me like defendants want to argue something  
25 about a freeze on the Exchange, but that's outside the



1 pleadings and not ripe for discussion.

2 One of the questions that I have with respect to fraud --  
3 and it applies, too, with respect to negligent  
4 misrepresentation, assuming that either or both of those can  
5 proceed -- is that it seems to me that those are personal  
6 claims. They are not class claims because you haven't pled  
7 reliance or justifiable reliance or an ability to address  
8 either of those individual issues in a class context.

9 So if all you're left with is fraud and negligent  
10 misrepresentation and/or negligence, how do you state a class  
11 claim for any of those individual torts?

12 **MR. CARRIEL:** We allege that the class in its entirety  
13 relied on these misrepresentations or omissions, rather,  
14 because it's a fraudulent concealment claim.

15 The notion here --

16 **THE COURT:** Well, fraudulent concealment you can only  
17 get there with a fiduciary duty. People don't have -- even in  
18 a 12 context, people don't have -- unless there is, again, a  
19 special relationship, omission claims are treated differently.  
20 So are you -- I thought you were proceeding on an affirmative  
21 claim. You're not?

22 **MR. CARRIEL:** I'm not sure that I understand the  
23 distinction that you're making.

24 **THE COURT:** An affirmative claim versus an omission?  
25 I affirmatively tell you something. "Mr. Carriel, it is

1 raining outside." I've affirmatively told you it is raining  
2 outside, and you go and you buy an umbrella, and it turns out  
3 it's a bright and sunny day, and you claim that I  
4 misrepresented the state of the weather to you to your damage  
5 of \$2 for buying an umbrella.

6 If I don't say anything and you go and you buy an umbrella  
7 and you realize it's a bright and sunny day and I knew perhaps  
8 that -- or maybe it would be different -- I'm not exactly  
9 sure -- but I don't have a duty to tell you anything unless  
10 there's some special relationship.

11 So if you're suing somebody on an affirmative basis, then  
12 you have to identify the actual misrepresentations upon which  
13 you are suing them, and I thought there were 36.

14 **MR. CARRIEL:** Yes, Your Honor.

15 **THE COURT:** If you're suing them for failing to tell  
16 you something, then you need to identify what the failure is  
17 and then you have to explain why they had a duty in the first  
18 place to explain that to you. That's an omission.

19 Do you understand the distinction?

20 **MR. CARRIEL:** Yes, Your Honor. And --

21 **THE COURT:** So what are you proceeding on?

22 **MR. CARRIEL:** Affirmative.

23 **THE COURT:** Okay.

24 **MR. CARRIEL:** Affirmatively fraudulently concealing  
25 the fact that the funds were not safe with affirmative

1 statements such as "your funds are safe" when they knew in fact  
2 that they were not safe.

3 **THE COURT:** So how do you get to justifiable reliance;  
4 that is, you don't have a statute -- typically in consumer  
5 fraud cases, there are statutes that -- and case law that talks  
6 about the manner in which class action can proceed with a  
7 reliance component because of a statute.

8 Reliance is an individual issue unless somehow explained  
9 otherwise. Someone could be sitting in this courtroom and  
10 invested and lost money. How is it that the plaintiff can tell  
11 me or can allege justifiable reliance for that person that they  
12 don't even know?

13 **MR. CARRIEL:** The justifiable reliance here is it is  
14 justified to rely on the word of the developers of XRB when  
15 they're discussing XRB.

16 **THE COURT:** So it sounds like you have nothing really  
17 personal or no other way of addressing the issue. This hasn't  
18 been briefed, but it concerns me.

19 Any response from the defense?

20 **MR. FOX:** Yes, Your Honor.

21 There are no allegations of reliance anywhere in this  
22 Complaint. There's no allegations that Mr. Fabian read a  
23 specific statement, that any specific statement influenced any  
24 decision either to purchase or to hold a Nano Coin. There is  
25 no identification of which specific statements are false.

1 Fraud in federal court needs to be pled under Rule 9(b),  
2 and if you look at footnote 154 of our opening brief, we cite  
3 case law for the proposition that in cases with respect to  
4 allegations of misrepresentations under Rule 9(b), the  
5 plaintiff needs to identify the specific statement that is  
6 alleged to be false, why it's false, the circumstances under  
7 which it was rendered, and who spoke. So in our view,  
8 Your Honor -- and this is in our papers -- they haven't  
9 properly alleged falsity.

10 To your prior point, they also haven't alleged reliance.  
11 They haven't alleged intent to defraud. It's anybody's guess  
12 why, assuming that these statements were false -- why the  
13 defendants intended to induce reliance. You need to read the  
14 whole pleadings backwards/forwards and take a guess. It's  
15 simply not spelled out, and under the relevant case law, it  
16 needs to be.

17 **THE COURT:** Well, if you have a business entity and  
18 the plaintiff alleges the names of the persons who made the  
19 statements and their authority to speak and who spoke and what  
20 they said, that's sufficient under California law with respect  
21 to that issue. Like I said, we have 36 statements specifically  
22 identified.

23 **MR. FOX:** My understanding from the pleadings -- and  
24 nothing to the contrary appears in the opposition brief -- is  
25 that the alleged misstatements have to do with BitGrail. There

1 are far fewer than 36 statements related to BitGrail.

2 In fact --

3 **THE COURT:** Well, there only has to be one.

4 **MR. FOX:** That's right. But I can -- if Your Honor  
5 will indulge me, I can walk you through the statements that  
6 were made during the relevant time period.

7 In fact, there are only two statements that were made  
8 prior to Mr. Fabian's final purchase of the coins related to  
9 BitGrail. They appear at paragraphs 112 and 114. That's a  
10 re-Tweet that says something to the effect of *XRB is now*  
11 *trading on BitGrail*. I don't understand that that's alleged to  
12 be false.

13 There's a statement on paragraph 117 in which one of the  
14 defendants says something to the effect of *if Nano can get into*  
15 *Blockfolio, coin holders will be able to track their losses and*  
16 *gains*. I don't believe that that's alleged to be false, and,  
17 in fact, it's a statement of opinion. That's it prior to his  
18 final purchase.

19 Now, after he purchased with respect to the theory that he  
20 was fraudulently induced to hold the coins, there are only two  
21 statements between his final purchase and January 12th, which  
22 is when, if Your Honor chooses to incorporate by reference the  
23 Italian bankruptcy decisions and if Your Honor does so, under  
24 *Davis vs. HSBC*, the Court should treat those decisions as part  
25 of the Complaint and accept all of the facts in those decisions

1 as true -- January 12th is the date when the accounts were  
2 frozen.

3 So there is only two statements --

4 **THE COURT:** Let me -- because I'm going to go back and  
5 look, but I find it hard to believe this notion that *Davis* says  
6 that all facts are to be stated as true, especially when  
7 they're someone's opinions on what facts may or may not be.

8 What is your jump cite for that specific claim which you  
9 have now made multiple times?

10 **MR. FOX:** I looked at it this morning. That is why  
11 I've made it.

12 If it is not on 1160, it is right around there because  
13 that's the passage in *Davis* that discusses the doctrine  
14 controlling incorporation by reference.

15 **THE COURT:** Yeah. But someone's opinion, it can't be  
16 a fact.

17 **MR. FOX:** Well, my interpretation of the case law  
18 would be that you would treat an opinion in a document that's  
19 incorporated by reference the same way you would treat an  
20 opinion that appears on the face of the Complaint. In other  
21 words --

22 **THE COURT:** But why? A plaintiff doesn't have to  
23 accept that. I can certainly accept as fact that an opinion  
24 was made and the date that it was made and that a trial  
25 happened and that certain evidence was taken, but to conclude

1 the conclusion of an individual that may be contrary to someone  
2 else's belief is not fact. It's opinion.

3 **MR. FOX:** My understanding is that the limit of *Davis*,  
4 what it stands for, is that the Court should -- once the Court  
5 decides to rely on matters that are incorporated by reference,  
6 the Court should treat those materials as though they were on  
7 the face of the Complaint.

8 **THE COURT:** It seems a stretch, but I'll look at it.

9 **MR. FOX:** If I may return to the two statements after  
10 the final purchase, one is at paragraph 109, and I believe that  
11 says something to the effect of *there are two hard-working*  
12 *gents trying to fix a problem*. Again, as far as I understand,  
13 not alleged to be false, and as with respect to all of these  
14 statements, there is no allegation that there was -- that  
15 Mr. Fabian ever read them or relied on them or that they  
16 affected his decision-making in any way.

17 And another one at paragraph 165, which also says  
18 something like *We're working on a problem with the node. All*  
19 *funds are safe*.

20 **THE COURT:** Okay.

21 **MR. FOX:** And with respect to this last one, again, no  
22 allegations of intent to defraud, no allegations of scienter,  
23 no allegations that the speaker knew that there was anything  
24 false about the statement, no allegations that Mr. Fabian read  
25 the statement, no allegations that he considered the statement

1 with respect to any decision that he was going to make.

2 And if Your Honor chooses not to rely on the Italian  
3 decisions, the other statements after January 12th are of the  
4 same vein.

5 **THE COURT:** Any comment?

6 **MR. CARRIEL:** Your Honor, defense counsel is trying to  
7 argue a securities fraud case under federal securities laws.  
8 We do not allege that there was fraud in connection with the  
9 purchase or sale of securities. We allege that after  
10 Mr. Fabian and the class purchased their XRB tokens, the Nano  
11 development team fraudulently concealed facts that they knew.  
12 This is not about misrepresentations in connection with the  
13 purchase or sale. So that is why there are no allegations of  
14 fraud prior to his purchase. That is irrelevant for our  
15 claims.

16 May I have my co-counsel step in to make one point?

17 **THE COURT:** One point.

18 **MR. FRIEDMAN:** Sure, Judge.

19 Paragraph 185 I direct the Court to. There is an express  
20 allegation right there that the plaintiff did rely on the  
21 truthfulness of all the representations set forth in the  
22 Complaint. After months of following the representations  
23 published by those people and relying on the truthfulness of  
24 their representations, Plaintiff Fabian began investing in XRB.

25 **THE COURT:** Which gets me back to the issue on



1 reliance.

2 **MR. FRIEDMAN:** Right.

3 **THE COURT:** Which is that paragraph 185 talks about  
4 the conduct of the plaintiff himself. You cannot make that  
5 representation on behalf of all the members of the class.

6 **MR. FRIEDMAN:** It may be a difficult claim to bring on  
7 behalf of the class, but certainly at this stage, what the  
8 plaintiff is arguing in this claim is very simple, and it is  
9 that beginning in July of 2017, the defendants became apprised  
10 that there was a significant problem, whether it be the problem  
11 of the Exchange by BitGrail or whether it be a problem with the  
12 Nano Node. There's an issue of fact there that certainly  
13 should resolve in favor of the plaintiffs at this stage. And  
14 that the defendants were apprised of that in writing, and that  
15 in the Italian bankruptcy decisions, there is reference that  
16 they were -- that the expert in that case saw a copy of a text  
17 message from Firano, the principal of the Exchange, to the Nano  
18 defendants telling them, "Guys, we have a problem here with our  
19 exchange and the listing and trading of XRB."

20 Notwithstanding that knowledge, we have various  
21 representations made by the Nano defendants on social media  
22 saying, "Don't worry. Your funds are safe." Saying, "Don't  
23 worry. We're working here on any issues that are popping up."  
24 And that there are multiple red flags throughout that are being  
25 either ignored or downplayed by the defendants.

1           **THE COURT:** Okay. And I would just note, though --  
2 and, again, you can respond to this -- paragraphs 183 through  
3 196 are all paragraphs relative to -- and you even say it -- to  
4 the lead plaintiff. It has nothing to do with the class.

5           **MR. CARRIEL:** Yes, Your Honor. However, reliance on a  
6 class-wide basis, we argue, is better dealt with at a later  
7 stage in the litigation such as class certification. At this  
8 point, we allege that the class of investors, which is all XRB  
9 holders on BitGrail, were justifiable in relying --

10           **THE COURT:** You have to have facts. That's a  
11 conclusion. You do have facts that you allege, 183 to 196.

12           **MR. CARRIEL:** We also have factual allegations that  
13 the Nano developers created XRB, and therefore any statement  
14 they made about XRB would have been relied upon and viewed by  
15 holders and investors.

16           **THE COURT:** Why would you think that? Why would you  
17 think that?

18           **MR. CARRIEL:** Because they invested in XRB so they are  
19 likely to trust the word of the creators of XRB.

20           **THE COURT:** How do you know? Okay.

21           Last claim -- constructive fraud again, it's going to rise  
22 and fall with the fiduciary issues because you need a  
23 confidential relationship.

24           The quasi-contract claim, I don't know how you can state  
25 this claim. There is no articulation of how the defendants

1 were enriched or that there's any benefit that was given to  
2 them that bears in some way on a claim for restitution which is  
3 how the unjust enrichment law is viewed for purposes of the  
4 common law.

5 So I don't know that that can survive because you haven't  
6 really alleged anything in that regard.

7 Anything else you want me to consider?

8 **MR. FOX:** Just very briefly, Your Honor, if I might be  
9 heard in rebuttal on the issue of fraud?

10 Mr. Carriel argued that we are arguing a federal  
11 securities fraud case with respect to the element of "in  
12 connection with a security." We are arguing California law.  
13 We are arguing the five fingers of fraud, the basic elements of  
14 fraud, that everybody learns in torts as a first-year law  
15 student. Reliance is an element.

16 If there is a misrepresentation, it needs to induce you to  
17 do something, and if it's not purchase the coin or hold the  
18 coin, I don't know what it is. So that's why we're talking  
19 about purchases and holding.

20 And, secondly, with respect to reliance, with respect to  
21 the allegations for Mr. Fabian's individual claim that appear  
22 around paragraph 180, 183, etc., that were just discussed, we  
23 would submit that those are not sufficient under Rule 9(b), and  
24 we would submit they are not sufficient under Rule 8 because  
25 they don't identify the specific statements on which Mr. Fabian

1 allegedly heard or relied. They don't provide any detail as to  
2 how they affected his decision-making. They're just  
3 boilerplate, of the type that the Supreme Court in *Iqbal* and  
4 *Twombly* has --

5 **THE COURT:** Well, on that point I would disagree with  
6 you. It used to be we would have 10-page Complaints. That's  
7 in the old days. Now this one is 67. Certainly much more than  
8 some of the stuff I've seen.

9 Okay. Anything else from the plaintiffs?

10 **MR. CARRIEL:** No, Your Honor.

11 **MR. FRIEDMAN:** There is one more thing, Your Honor.

12 With regard to the negligence claim that the plaintiffs  
13 are bringing, it is more multifaceted than simply the issue  
14 with the dispute between whether the Nano Node has a problem or  
15 whether the BitGrail Exchange has a problem.

16 The negligence ties into exactly what I spoke about  
17 previously on the fraud claim with regard to the defendants  
18 becoming apprised of the issue and failing to disclose that on  
19 social media. It has to do with the defendants making  
20 representations that everything is fine on social media. It  
21 also has other facets, including making representations about  
22 hanging on to and holding XRB. For example, we've alleged --

23 **THE COURT:** Okay. Look, first of all, we've already  
24 done that.

25 Second of all, now you really are talking about negligent

1 misrepresentation, not negligence, because negligence, there  
2 has to be a duty to do a particular thing which caused damage.  
3 Now you're arguing that they said things which -- anyway, I  
4 think --

5 **MR. CARRIEL:** That's right, Your Honor.

6 **THE COURT:** -- you're conflating issues and --

7 **MR. FRIEDMAN:** I may be, but I only mean it to say  
8 that it is multifaceted to the extent that not only did they  
9 make misrepresentations, they also -- the defendants are  
10 alleged to have forcibly kept the BitGrail Exchange open and  
11 kept it open for trading when these problems were occurring and  
12 after the defendants had knowledge of it. Those are  
13 allegations in the Complaint.

14 There are allegations that the defendants hosted chat  
15 rooms. However, that, again, would tie into the  
16 misrepresentations.

17 But the overarching point, Your Honor, is that the  
18 defendants failed to act reasonably consistent with a  
19 reasonable duty of care to simply either apprise holders of  
20 these tokens, that there was a problem on the Exchange, or to  
21 remove -- or to stop trading on the Exchange or to even conduct  
22 the security audit of the Exchange a year after they were  
23 apprised that the Exchange had a problem. They did nothing.

24 So they failed to act, they failed to apprise the public,  
25 so there's a host of reasons why there is a negligence claim

1 available.

2 **THE COURT:** All right. Thank you, Gentlemen.

3 **MR. SCHOOLIDGE:** Thank you, Your Honor.

4 **MR. FOX:** Thank you, Your Honor.

5 (Proceedings adjourned at 3:14 p.m.)

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CERTIFICATE OF REPORTER

I certify that the foregoing is a correct transcript  
from the record of proceedings in the above-entitled matter.

DATE: Wednesday, October 23, 2019

*Pamela Batalo Hebel*

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Pamela Batalo Hebel, CSR No. 3593, RMR, FCRR  
U.S. Court Reporter